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NO. 91-539

In The
SUPREME COURT OF THE UNITED STATES
October Term 1991

DONALD LORD,

Petitioner,

vs.

FARM CREDIT BANK OF ST. PAUL
f/k/a Federal Land Bank of
St. Paul and RICHARD HOBL,

Respondents.

On Petition For a Writ of
Certiorari to the Supreme Court
for the State of Wisconsin

BRIEF FOR THE RESPONDENT RICHARD HOBL IN OPPOSITION

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STATEMENT OF THE CASE

The respondent, Farm Credit Bank of St. Paul f/k/a Federal Land Bank of St. Paul (hereinafter "Farm Credit"), obtained a judgment foreclosing its mortgage on real estate owned by Donald Lord (hereinafter "Lord") in the Circuit Court for Taylor County, Wisconsin on December 23, 1987. That judgment determined the amount of the mortgage debt, with interest, costs and attorney's fees to be $127,959.59. (R. 3, p. 2)[1] After the redemption period of Wisconsin Statute section 846.13 expired, Farm Credit scheduled a foreclosure sale for February 14, 1989. (R. 4) However, Lord filed a Chapter 7 bankruptcy petition in the Bankruptcy Court for the Western

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[1] Indicates record on appeal in the Wisconsin Supreme Court.

District of Wisconsin. After relief from stay was obtained, the foreclosure sale was adjourned and renoticed for March 28, 1989. (R. 7) The foreclosure sale was again adjourned and renoticed for April 25, 1989. (R. 12) Respondent, Richard Hobl (hereinafter "Hobl") was the successful bidder at the sheriff's sale. Hobl's successful bid was $50,000.00. Lord attended the foreclosure sale but, upon instructions from his attorney, did not bid. (R. 49, p. 16) Hobl was the only bidder at the sheriff's sale. (R. 49, p. 7) The Taylor County Sheriff filed his Report of Sale on April 27, 1989, and on May 30, 1989, Farm Credit moved the trial court for confirmation of the sale. (R. 14)

Lord was discharged in bankruptcy on June 2, 1989. (R. 15, p. 13) On the day of the confirmation hearing (June 14,

1989), Lord, without prior notice to the interested parties, filed a motion to permit redemption for $50,000.00 (the price bid at the sheriff's sale) and paid that amount in to the trial court. (R. 49, p. 14) Lord argued that because of his bankruptcy discharge the *in personam* judgment against him was satisfied and that all that remained was the *in rem* action against the property serving as security for the discharged debt. (R. 15, p. 1) As a result, Lord argued that he should be entitled to redeem for $50,000.00, the amount of the successful bid. (R. 15, p. 1)

Prior to this, Lord filed an adversary proceeding in his Chapter 7 bankruptcy requesting an evaluation pursuant to 11 U.S.C. sec. 506 and redemption of the subject matter real estate. The Bankruptcy Court entered an

order on May 23, 1989 finding that the present value of the real estate was $48,000.00 and took under advisement Lord's requested evaluation and redemption and a motion filed by Farm Credit to dismiss.[2] The Bankruptcy Court never ruled on Lord's request for redemption and on July 23, 1991 dismissed the adversary proceeding. (See appendix)

The trial court heard Farm Credit's motion for confirmation of the sale and Lord's motion to redeem the property on June 14, 1989. The trial court permitted Lord to redeem the property for the $50,000.00 bid price plus the payment of delinquent taxes despite Wisconsin Statute section 846.13, which requires

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[2]Lord's arguments in his petition are prefaced on his assumption that the Bankruptcy Court ordered a strip-down of Farm Credit's mortgage. It is clear that the court did not do so but merely took Lord's request under advisement.

payment of the full foreclosure judgment to redeem. The trial court denied confirmation of the sheriff's sale. (R 49, p. 25)

Hobl appealed the trial court's decision to the Wisconsin Court of Appeals, District III. On June 5, 1990, the Court of Appeals released its 2-1 decision affirming the trial court. Hobl v. Lord, 157 Wis.2d 13, 458 N.W.2d 536 (Ct. App. 1990)

The majority of the Wisconsin Court of Appeals perceived a conflict between Section 506 of the Bankruptcy Code, 11 U.S.C. 506, and Wisconsin Statute section 846.13. It held that the term "judgment", as used in Wisconsin Statute section 846.13, means the amount of the judgment that survives bankruptcy proceedings and held that Lord had properly redeemed by paying the stripped-

down amount.

Hobl petitioned the Wisconsin Supreme Court to review the decision of the Wisconsin Court of Appeals. The Wisconsin Supreme Court granted the petition to review, and on June 5, 1991, unanimously reversed the lower courts. Hobl v. Lord, 162 Wis.2d 226, 470 N.W.2d 265 (1991).

In so doing, the Wisconsin Supreme Court reviewed the case law concerning strip-downs under 11 U.S.C. sec. 506. Specifically, it reviewed In re Dewsnup, 908 F.2d 588 (10th Cir. 1990), cert. granted _____ U.S. _____, 111 S.Ct. 949, (1991); In re Lindsey, 823 F.2d 189 (7th Cir. 1987); Gaglia v. First Federal Savings and Loan, 889 F.2d 1304 (3rd Cir. 1989); Matter of Folendore, 862 F.2d 1537 (11th Cir. 1989); and In re Zobencia, 109 B.R. 814 (Bankr. W.D. Tenn 1990).

After reviewing those cases, the Wisconsin Supreme Court correctly concluded that section 506 of the Bankruptcy Code does not operate to permit a debtor to redeem real estate. As such, the court continued, there is no conflict between the redemption provision of Wisconsin Statute section 846.13 and federal law. The court further found that to allow a redemption at the stripped-down value, given the terms of Wisconsin Statute section 846.13, was contrary to public policy and could devastate this country's banking system.

From this decision of the Wisconsin Supreme Court Lord petitions the United States Supreme Court for a writ of certiorari.

SUMMARY OF ARGUMENT

Review by the United States Supreme Court of the Wisconsin Supreme Court's

decision is not warranted. In federal bankruptcy proceedings property rights are determined by state law except when in conflict with the Bankruptcy Code. Butner v. United States, 440 U.S. 48 (1979). Wisconsin Statute section 846.13 is Wisconsin's mortgage redemption statute. Section 506 of the Bankruptcy Code, 11 U.S.C. section 506, is the subject of much debate in the courts of this country. A vigorous split of authority exists as to whether a Chapter 7 debtor can use section 506 to strip down real estate mortgages. That issue is currently before this court in In re Dewsnup, supra. Every Court of Appeals' decision which has determined this issue, however, both pro and con, has specifically determined that section 506 is not a redemption provision. There is, therefore, no conflict between section

506 of the Bankruptcy Code and Wisconsin Statute section 846.13. As a result, it is inappropriate for this court to grant Lord's petition for a writ of certiorari. 28 U.S.C. section 1257; Sup. Ct.R. 10.1(b)(c).

REASONS FOR DENYING THE WRIT

Lord curries the favor of this court's writ of certiorari by arguing that the Wisconsin Supreme Court has trampled on federal law. At the heart of his arguments are two statutes: section 506 of the Bankruptcy Code, 11 U.S.C. section 506, and section 846.13 of the Wisconsin Statutes. Section 506 of the Bankruptcy Code provides for bifurcation of a creditor's claim into a secured and an unsecured portion. See United States v. Ron Pair Enterprises, Inc., 489 U.S. 235, n. 3 (1989). In Chapter 7 proceedings, its use (which has been

coined a "strip down") as to real estate mortgages has generated a split of authority among the Circuit Courts of Appeal and among the Bankruptcy Courts. That issue is presently before this court on certiorari from the Tenth Circuit. In re Dewsnup, supra. Wisconsin Statute section 846.13 is Wisconsin's real estate redemption statute. It provides that a mortgagor must pay the entire amount of the foreclosure judgment plus post-judgment interest, costs and taxes to redeem.

At the onset, it is important to note that the issue before this court in Dewsnup is distinct from the issue presented for consideration by Lord in this case. The issue in Dewsnup, simply put, is whether a Chapter 7 debtor may utilize section 506 to strip-down a real estate mortgage. The issue presented

here is whether section 506 is a real estate redemption provision that preempts Wisconsin Statute section 846.13.[3]

The issue Lord would like this court to entertain is one of the relationship between federal bankruptcy law and state property law. This court has explained that relationship most recently in Butner v. United States, supra. Butner considered whether the right to rents collected during the period between the mortgagor's bankruptcy and the foreclosure sale of the mortgaged premises was to be determined by a federal rule of equity or state law. In finding that the state law controlled, Justice Stevens, for a unanimous court,

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[3]Lord's arguments are, however, prefaced on the assumption that a Chapter 7 debtor can strip-down a real estate mortgage under 11 U.S.C. 506. If this court affirms Dewsnup, supra., his argument fails.

states:

> "Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interest should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a state serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving 'a windfall' merely by the happenstance of bankruptcy."
>
> 440 U.S. at 55. (Citation omitted)
>
> * * *
>
> "What does follow is that the federal bankruptcy court should take whatever steps are necessary to ensure that the mortgagee is afforded in federal bankruptcy court the same protection he would have under state law if no bankruptcy had ensued."
>
> 440 U.S. at 56.

See also: Stellwagen v. Clum, 245 U.S. 605 (1918); Sturges v. Crowninshield, 4 Wheat. 122 (1819); and Ogden v. Saunders, 12 Wheat. 213 (1827).

This relationship has been echoed in

Johnson v. First National Bank of Montevideo, 719 F.2d 270 (8th Cir. 1983), cert. denied, 465 U.S. 1012 (1984). In that case, the Eighth Circuit Court of Appeals was confronted with the question of whether a bankruptcy court had the authority to toll the running of the Minnesota statutory redemption period. In holding that a bankruptcy court does not have this power, the Eighth Circuit states:

> "Article 1, Section 8 of the United States Constitution provides that Congress shall have the power to establish uniform bankruptcy laws throughout the United States. Where Congress has chosen to exercise its authority, contrary provisions of state law must accordingly give way. It is equally well settled, however, that state laws are suspended only to the extent of actual conflict with the bankruptcy system provided by Congress, so that in the absence of any conflict between the state and bankruptcy laws, the law of the state where the property is situated governs questions of property rights."
>
> 719 F.2d at 273 (Citations omitted)

* * *

> "* * * From the fundamental principles embraced by the Butner opinion, however, . . . it follows that, absent a specific grant of authority from Congress or exceptional circumstances, a bankruptcy court may not exercise its equitable powers to create substantive rights which do not exist under state law."

719 F.2d at 274 (Citations omitted)

Another case dealing with state redemption rights and the rationale of Butner v. United States, supra., is Justice v. Valley National Bank, 849 F.2d 1078 (8th Cir. 1988). In Justice, the debtors filed a Chapter 12 bankruptcy petition following a foreclosure sale but before the expiration of the South Dakota statutory redemption period. In their Chapter 12 plan the debtors proposed to pay the redemption amount over time, which would have the effect of extending the state statutory redemption period.

The debtors argued that under sections 1222(b)(3) and (5) of the Bankruptcy Code, 11 U.S.C. sec. 1222(b)(3),(5), they should be allowed to cure or waive any default, and in their minds, this would include "curing" their state redemption rights by paying the redemption amount over time. In denying the debtors' request, the court held that section 1222(b)(3) and (5) of the Bankruptcy Code did not conflict with the state law on redemption, and held that the state law controlled the rights of the parties regarding redemption. Its comments are noteworthy:

> "Finally, substantial state interests support the application of local law in this context. In addition to the general values promoted by uniform intrastate treatment of property interests, . . . each state has its own well-developed system of real property law, which 'reflect[s] important and carefully evolved state arrangements designed to serve multiple purposes . . .' These systems have no

> federal counterpart, and we are therefore reluctant to 'invent one and impose it upon the states . . .' Lenders and borrowers depend on local property law 'to provide the stability essential for reliable evaluation of the risks involved' in mortgage transactions . . . Absent a clear congressional directive, we should not create new rules and generate additional uncertainties whose ultimate consequences may be difficult to foresee."
>
> 849 F.2d at 1088 (Citations and footnote omitted)

The relationship of state redemption law and federal bankruptcy law was also faced in DeMers v. Federal Land Bank of Omaha, 89 B.R. 48 (C.D.S.D. 1987). The Chapter 11 debtors in that case sought to redeem their foreclosed real estate by paying the redemption amount over time. The only problem was that the South Dakota redemption statute provided for paying the redemption price in one lump sum. The court, following the wisdom of Butner v. United States, supra., held that the debtors could not redeem the

property by paying the redemption amount over time. It respected the state law on redemption requiring a lump-sum payment.

The respect given by the bankruptcy courts to state property law oftentimes results in a bankruptcy court in one state ruling differently on an issue than a bankruptcy court in another state. This court recognizes that reality:

> "Notwithstanding this requirement as to uniformity the bankruptcy acts of Congress may recognize the laws of the State in certain particulars, although such recognition may lead to different results in different States. For example, the Bankruptcy Act recognizes and enforces the laws of the States affecting dower, exemptions, the validity of mortgages, priorities of payment and the like. Such recognition in the application of state laws does not affect the constitutionality of the Bankruptcy Act, although in these particulars the operation of the act is not alike in all the States."
>
> Stellwagen v. Clum, supra. at 613.

A classic example of this is the issue of whether a Chapter 13 debtor can cure a

default and reinstate a home mortgage where the Chapter 13 petition is filed during the state redemption period but after foreclosure and sale. Matter of Roach, 824 F.2d 1370 (3rd Cir. 1987) respecting New Jersey foreclosure law says "no", while In re Clark, 738 F.2d 869 (7th Cir. 1984) respecting Wisconsin foreclosure law says "yes".

With this background, the question in this case becomes whether there is any federal interest that needs protection by the United States Supreme Court. Put more succinctly, whether there is any conflict between the provisions of section 506 of the Bankruptcy Code and Wisconsin Statute section 846.13. As the Wisconsin Supreme Court in this case has noted, there is no such conflict.

As mentioned above, the issue of whether a Chapter 7 debtor can utilize

section 506 to strip-down a real estate mortgage has sharply divided the bankruptcy courts around the country. The circuit courts that have decided the strip-down issue, however, both pro and con, are unanimous in declaring that section 506 is not a redemption provision.

Gaglia v. First Federal Savings & Loan, supra., which holds that a debtor can strip-down a real estate mortgage, states:

> "Section 506, however, is not a redemption provision. Even after lien avoidance, the [debtors] will not own the property unencumbered. They will still be subject to [the first mortgagee's] mortgage and the [second mortgagee's] claim to the extent it is secured. If the [debtors] are delinquent on the first mortgage, [the first mortgagee] has the right to foreclose, even if they can satisfy the [second mortgagee's] secured claim against the remaining equity."
>
> 889 F.2d at 1310 (Emphasis added)

Matter of Folendore, supra., which

also allows a real estate mortgage strip-down, states:

> "Section 506(d) does not really 'redeem' the property of the debtor. The [debtors'] only interest in the property is possession--the two [senior mortgagees] effectively own the property. While it is true that the [debtors] might in the future pay off the mortgages on the property, at this moment the [senior mortgagees] could foreclose on the property and cut the [junior mortgagee] and the [debtors] out completely."
>
> 862 F.2d at 1540 (Emphasis added)

In re Lindsey, supra., which can be (and has been) read to allow a strip-down of a real estate mortgage, states:

> ". . . [B]ut once the strip-downs were complete and the secured claims allowed in their stripped-down amount . . . the only thing that remained to do in the bankruptcy proceeding was to discharge the debtors and let the creditors foreclose their stripped-down liens, subject to whatever rights of redemption the debtors might have, under state law, in the foreclosure proceedings."
>
> 823 F.2d at 191 (Emphasis added)

In re Dewsnup, supra., now before

this court, rejects the notion that section 506 can be used to strip-down a real estate mortgage. The Tenth Circuit, in so doing, notes that the Bankruptcy Code's only redemption provision available to a Chapter 7 debtor is 11 U.S.C. 722, which only applies to personal property. With this in mind, the court states that "it is obvious that Congress did not intend to permit a debtor to redeem his real property through the use of section 506(d)." 908 F.2d at 592 quoting In re Maitland, 61 B.R. 130, 135 (Bankr. E.D. Va. 1986). Dewsnup also notes that its holding does not alter the available remedies which the debtors may have. Id., n. 3.

In addition to the Circuit Court of Appeals, a number of bankruptcy courts that have allowed strip-downs take pains to proclaim that section 506 is not a

redemption provision. In re Zlogar, 101 B.R. 1 (Bankr. N.D. Ill. 1989) states:

> "Section 506 only determines the status of the secured claim and does not determine the rights of a debtor and its creditors with respect to any disposition of the property. Therefore, where a debtor wants to retain ownership of property in a chapter 7 case, application of section 506 is but one step in what will be at least a two-step process. This first step is limited to determining the status of secured claims and what liens remain on the property. The manner of enforcement of those liens remaining after section 506(d) has been applied is a separate question, and a second step, which turns on applicable state law."
>
> 101 B.R. at 8.
>
> * * *
>
> "In light of Lindsey, allowing the Debtor to avoid the liens on her interest in the property to the extent that the liens exceed the value of that property does not necessarily work a redemption. Whether or not the Debtor can redeem or otherwise retain her interest in the property depends on state law applicable to the agreement between the Debtor and whoever emerges as a secured creditor after the section 506(d) hearing."

101 B.R. at 10 (Citation omitted)

Lord cites In re Zobencia, 109 B.R. 814 (Bankr. W.D. Tenn, 1990) but fails to relate that Zobencia recognizes that section 506 of the Bankruptcy Code is not a redemption provision. Zobencia states:

> "The Court recognizes that there is no Bankruptcy Code authorization for redemption of realty. Compare section 722 (permitting redemption at the 'amount of the allowed secured claim' on personal property only). Section 506 is not a redemption statute. . . . The strip down provisions of section 506 merely put the parties in the same position they would be in the event of liquidation, leaving these creditors with no more or less expectation for recovery than they would enjoy at foreclosure."

109 B.R. at 821 (Citations omitted)

Zobencia went on, however, to allow the debtors to pay off the first mortgage and to pay the stripped-down amount to the second mortgagor within 30 days. The court made such an order by reasoning it would merely put the parties in the same

position as they would be under Tennessee law on redemption. If the debtors did not pay within this time period, the mortgagees were permitted to foreclose their mortgages without further court order.

At first blush, the Zobencia holding is confusing. After all, it states that section 506 of the Bankruptcy Code is not a redemption statute but then allows the debtors to pay the stripped-down amount to get the property back. Upon close examination, however, it is consistent. Zobencia states that it is allowing the debtors to make this payment because it puts the parties in the same position they would be under Tennessee's redemption law. Under Tennessee law, a mortgagor can redeem after sale by paying to the purchaser the amount bid at the sale (plus interest and costs).

Tennessee Code Annotated 66-8-101 et. seq. As such, Zobencia allowed the debtors to pay the stripped-down amount as a matter of practicality.

Another case which recognizes the non-redemptive features of section 506 of the Bankruptcy Code and its lack of impact on state law is In re O'Leary, 75 B.R. 881 (Bankr. D. Ore. 1987). There the court allowed a strip down, but stated:

> "Here, allowing the plaintiffs to void the defendant's mortgage on their residence to the extent that the claim secured by the mortgage is unsecured does not necessarily work a redemption. '. . . in a Chapter 7 liquidation proceeding the Court has no authority to rewrite the terms and conditions of the security agreement.' . . . Whether or not the plaintiffs could 'redeem' their residence from defendant's mortgage by payment, to defendant, in the sum of $29,000, might well depend upon the provisions of the note and mortgage existing between plaintiffs and defendant (for example, there could be pre-payment penalties and other contractual obligations that would remain unaltered by fixing

defendant's allowed secured claim under section 506.)"

75 B.R. 884 (Citation omitted)

If judicial construction of section 506 of the Bankruptcy Code cannot rewrite the contract between the parties, it obviously cannot rewrite state redemption laws.

As is clear from the above, section 506 of the Bankruptcy Code is not a redemption provision.

What Lord asks this court to do is to basically invent a redemption provision for real estate in the Bankruptcy Code and then declare that this heretofore unknown redemption provision preempts Wisconsin Statute section 846.13. Such a request is not unlike the scenario faced by this court in Auto Workers v. Hoosier Cardinal Corporation, 383 U.S. 696 (1966). There the plaintiff brought an action under

section 301 of the Labor Management Relations Act, 29 U.S.C. 183, for unpaid vacation pay. The lower courts dismissed the action as untimely under the applicable state statute of limitations. The Labor Management Relations Act contained no limitations provision for such an action. The plaintiff urged this court to adopt a uniform federal statute of limitations in light of Congress' silence in that regard. In refusing that request, this court stated:

> "That Congress did not provide a uniform limitations provision for section 301 suits is not an argument for judicially creating one, unless we ignore the context of this legislative omission. It is clear that Congress gave attention to limitations problems in the Labor Management Relations Act, 1947; it enacted a six months' provision to govern unfair labor practice proceedings, 61 Stat. 146, 29 U.S.C. section 160(b) (1964 ed.), and it did so only after appreciable controversy. In this context, and against the background of the relationship between Congress and the courts on the question of

> limitation provisions, it cannot be fairly inferred that when Congress left section 301 without a uniform time limitation, it did so in the expectation that the courts would invent one."

383 U.S. at 703 (Footnote omitted)

The "context of the legislative omission" is just as strong here as in Auto Workers. Congress has specifically created a redemption provision for personalty in Chapter 7 cases, 11 U.S.C. 722, and is silent as to a redemption provision for real estate. That silence cannot be used to infer that Congress left a real estate redemption provision up to the courts to create. To the contrary, Congress' silence indicates that redemption of real estate is to be governed by the applicable state law.

With no federal real estate redemption provision, there is no conflict between federal law and Wisconsin Statute section 846.13. It

follows then, under the teaching of Butner v. United States, supra, that Wisconsin's redemption law is to be followed as there is no federal interest to protect. It also follows that this case is not appropriate for certiorari.[4]

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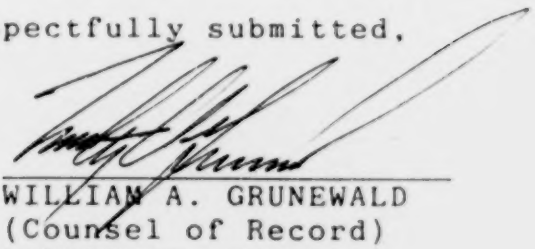
[4] In his petition for writ of certiorari, Lord, in addition to arguing that section 506 of the Bankruptcy Code preempts Wisconsin's redemption statute, plays the hand of "fairness" and "fresh start." Lord basically argues that it is unfair that he has to pay the judgment amount to redeem the mortgaged premises while Hobl can purchase the mortgaged premises for the amount of his bid. How such an argument is pertinent to whether or not this court entertains this case escapes respondent's perception. The argument ignores the fact that under Wisconsin Statute section 846.10(2) any party, including Lord, may bid at a sheriff's sale. Lord attended the sheriff's sale but, on the instructions on his attorney, did not bid. If he wanted to retain the mortgaged premises, his avenue to do so was the bidding process. This bidding process also preserves his "fresh start."

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,



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October 28, 1991

APPENDIX

UNITED STATES BANKRUPTCY COURT

WESTERN DISTRICT OF WISCONSIN

In re: Case Number:

DONALD LORD, EU7-89-00332

Debtor.

DONALD LORD,

Plaintiff, Adversary Number:

v. 89-0062-7

FARM CREDIT BANK OF ST. PAUL, a/k/a Federal Land Bank of St. Paul; and ESTATE OF IDA LORD, ORDER

Defendants.

Defendant Farm Credit Bank of St. Paul having previously moved to dismiss this adversary proceeding, and the motion having been held open at request of the parties pending resolution of related

state court litigation now apparently completed, and any remaining issues herein appearing moot,

NOW, THEREFORE, IT IS ORDERED that the motion of defendant Farm Credit Bank of St. Paul to dismiss is granted, and this adversary proceeding is hereby dismissed.

Dated: July 23, 1991.

BY THE COURT:

HON. THOMAS S. UTSCHIG
U.S. Bankruptcy Judge